

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky
REPORT OF AUDIT
Year Ended June 30, 2013

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Marr, Miller & Myers, PSC

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INDEPENDENT AUDITOR'S REPORT

October 7, 2013

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Middlesboro Independent School District (the "District"), as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with U.S. generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; the provisions of Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations; Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the Independent Auditor's Contract – State Audit Requirements, Appendix III to the Independent Auditor's Contract – Audit Extension Request and Appendix IV to the Independent Auditor's Contract – Instructions for Submission of the Audit Report. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the District as of June 30, 2013, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis and budgetary comparison information on pages 4-7 and 14-15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with U.S. generally accepted auditing standards, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements, and statistical section, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole.

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The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 7, 2013, on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Marr, Miller & Myers, PSC

Certified Public Accountants

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013

The management of the Middlesboro Independent School District (District) offers readers this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2013. We encourage readers to review the information presented here in conjunction with additional information found within the body of the audit.

SUPERINTENDENT'S REVIEW OF THE YEAR

During the year ended June 30, 2013, the Middlesboro Independent School District had made several decisions that had a direct impact on the end of the year financial balance. Since we are scheduled to receive less SEEK funding and because we are declining in enrollment, it was evident that we needed to re-adjust our spending to guarantee an appropriate fiscal balance in succeeding years. Some of the steps initiated by the District were to assess our current level of staffing and evaluate all transportation costs for the District.

Overall, this has been a financially successful year for the District. Although our funding from federal and state sources decreased, and continues to diminish, we have been able to maintain our overall fund balance. This is especially critical due to continuing financial shortfalls of federal and state funding.

FINANCIAL HIGHLIGHTS

- The ending cash balance for the District was \$130,232 in 2013 and \$381,624 in 2012. The cash balances include \$93,475 and \$40,202 for 2013 and 2012, respectively, reserved for debt service payments, and \$10 and \$124,510 for 2013 and 2012, respectively, reserved for future construction projects.
- The General Fund had \$10,388,686 in revenue, excluding interfund transfers and compensation for loss of assets, which primarily consisted of the state program (SEEK) and property, utilities, and motor vehicle taxes. Excluding interfund transfers, there were \$10,354,288 in General Fund expenditures.
- When funds are available, the District may use cash or sell bonds to build or renovate facilities within the school district. The projects must be identified on the District Facility Plan.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The statement of net position presents information on all of the District's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statement of activities presents information showing how the District's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013

The government-wide financial statements outline functions of the District that are principally supported by property taxes and intergovernmental revenues (governmental activities). The governmental activities of the District include instruction, support services, operation and management of plant, student transportation and operation of non-instructional services. Fixed assets and related debt is also supported by taxes and intergovernmental revenues.

The government-wide financial statements can be found on pages 8 and 9 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. This is a state mandated uniform system and chart of accounts for all Kentucky public school districts utilizing the MUNIS administrative software. The District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the District can be divided into three categories: governmental, proprietary and fiduciary. Fiduciary funds are trust funds established by benefactors to aid in student education, welfare and teacher support. The proprietary fund is vending and food service operations. All other activities of the District are included in the governmental funds.

The basic governmental fund financial statements can be found on pages 10 through 13 of this report.

Notes to the basic financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found on pages 20 through 35 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The largest portion of the District's net assets reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, vehicles, general equipment and construction in progress); less any related debt used to acquire those assets that are still outstanding. The District uses these capital assets to provide services to its students; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The District's financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

Net Position for the period ending June 30, 2013

Fiscal year 2013 government-wide net position compared to 2012 is as follows:

	2013	2012
Current assets	\$ 943,691	\$ 1,019,102
Capital assets	<u>6,256,264</u>	<u>6,527,431</u>
Total Assets	<u>\$ 7,199,955</u>	<u>\$ 7,546,533</u>
Current liabilities	\$ 596,565	\$ 893,975
Noncurrent liabilities	<u>2,653,692</u>	<u>2,810,272</u>
Total Liabilities	<u>\$ 3,250,257</u>	<u>\$ 3,704,247</u>
Net position		
Investment in capital assets, net of related debt	\$ 3,300,419	\$ 3,155,954
Restricted	430,187	672,303
Unrestricted	<u>219,092</u>	<u>14,029</u>
Total Net Position	<u>\$ 3,949,698</u>	<u>\$ 3,842,286</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013

The District had an overall increase in total net position of \$107,412, comprised of a decrease in business-type activities of \$20,432 and an increase in governmental activities of \$127,844.

The following table presents a summary of revenues and expenditures, Governmental Funds only, for the fiscal years ended June 30:

	<u>2013</u>	<u>Percent</u>	<u>2012</u>	<u>Percent</u>
REVENUES				
Local revenue sources	\$ 3,057,066	22.75 %	\$ 2,822,915	20.10 %
State revenue sources	8,543,742	63.58	8,826,020	62.84
Federal sources	<u>1,836,973</u>	<u>13.67</u>	<u>2,396,699</u>	<u>17.06</u>
Total revenues	<u>13,437,781</u>	<u>100.00</u>	<u>14,045,634</u>	<u>100.00</u>
EXPENDITURES				
Instruction	7,763,721	57.78	8,887,383	63.28
Student support services	534,508	3.98	557,237	3.97
Instructional staff	844,175	6.28	851,954	6.07
District administration	641,219	4.77	625,751	4.46
School administration	835,367	6.22	834,799	5.94
Business	176,354	1.31	169,236	1.20
Plant operations and maintenance	1,223,917	9.11	1,525,432	10.86
Student transportation	505,770	3.76	532,469	3.79
Architectural/engineering	103,553	.77	102,508	.73
Community services activities	186,418	1.39	196,638	1.40
Debt service/lease obligations	<u>688,866</u>	<u>5.13</u>	<u>709,736</u>	<u>5.05</u>
Total expenditures	<u>13,503,868</u>	<u>100.50</u>	<u>14,993,143</u>	<u>106.75</u>
Excess revenues (expenditures)	<u>\$ (66,087)</u>	<u>(.50)%</u>	<u>\$ (947,509)</u>	<u>(6.75)%</u>

The majority of the District's revenue was derived from state revenue sources making up 63.58% of their revenue in 2013 as compared to 62.84% in 2012. Local revenue sources comprised 22.75% of total revenue in 2013 as compared to 20.10% in 2012.

Instructional expenditures comprised 57.78% of the District's expenses for 2013 as compared to 63.28% in 2012. Plant operations and maintenance was the next largest consumption of revenues at 9.11% in 2013 as compared to 10.86% in 2012.

Comments on Budget Comparisons

In Kentucky, the public schools fiscal year is July 1 to June 30. Other programs operate on a different fiscal calendar, but are reflected in the District's overall budget. By law, the budget must have a minimum 2% contingency. The District adopted a 2012-13 budget with \$339,334 in contingency (2.76%).

- The District's total general fund revenues for the fiscal year ended June 30, 2013 were \$10,388,686.
- General fund budgeted revenue compared to actual revenue varied from line item to line item with the ending actual balance being \$2,017,843 more than budget or 24.11%. This is due primarily to recording on-behalf payments made by the State of Kentucky of \$1,910,110 that were not budgeted. When these are eliminated, revenues compared to budget were \$107,733 or 1.24% more than anticipated.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013

- The total cost of all general fund programs and services for the fiscal year ended June 30, 2013 were \$10,354,288.
- General fund budgeted expenditures compared to actual expenditures varied from line item to line item with the ending actual balance being \$1,523,821 more than budget or 17.26%. This is due primarily to recording on-behalf payments made by the State of Kentucky of \$1,910,110 that were not budgeted. When these are eliminated, expenditures compared to budget were \$386,289 or 4.37% less than anticipated.

FUTURE BUDGET IMPLICATIONS

In Kentucky, the public schools fiscal year is July 1 to June 30; other programs, i.e. some federal programs, operate on a different fiscal calendar, but are reflected in the District's overall budget. By law, the budget must have a minimum 2% contingency. The District adopted a 2013-14 budget with \$417,284 in contingency (3.6%). Board action that impacts the finances includes:

- Expanding technology.
- Board match on Offers of Assistance from SFCC and Technology.
- Maintaining current staff levels.

Contacting the District's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives.

Questions regarding this report should be directed to the Superintendent or to Ava Wilder, Director of Financial Services (606) 242-8800 or by mail at 220 North Twentieth Street, Middlesboro, KY 40965.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF NET POSITION
June 30, 2013

<u>ASSETS</u>	Governmental <u>Activities</u>	Business-Type <u>Activities</u>	<u>Total</u>
CURRENT ASSETS			
Cash and cash equivalents	\$ 233,789	\$ (103,557)	\$ 130,232
Accounts receivable:			
Taxes – current	137,090	-	137,090
Accounts receivable	23,669	2,917	26,586
Intergovernmental – state	6,712	-	6,712
Intergovernmental – federal	523,010	101,691	624,701
Materials and supplies inventory	-	14,793	14,793
Prepaid expenditures	3,577	-	3,577
Total current assets	<u>927,847</u>	<u>15,844</u>	<u>943,691</u>
NONCURRENT ASSETS			
Capital assets, net	<u>6,182,217</u>	<u>74,047</u>	<u>6,256,264</u>
Total noncurrent assets	<u>6,182,217</u>	<u>74,047</u>	<u>6,256,264</u>
TOTAL ASSETS	<u>7,110,064</u>	<u>89,891</u>	<u>7,199,955</u>
 <u>LIABILITIES AND NET POSITION</u>			
CURRENT LIABILITIES			
Accounts payable	114,765	8,069	122,834
Accrued salaries and benefits payable	21,022	4,249	25,271
Deferred revenue	146,307	-	146,307
Current portion of bond obligations	245,000	-	245,000
Current portion of lease obligations	57,153	-	57,153
Total current liabilities	<u>584,247</u>	<u>12,318</u>	<u>596,565</u>
NONCURRENT LIABILITIES			
Noncurrent portion of bond obligations	2,425,000	-	2,425,000
Noncurrent portion of lease obligations	228,692	-	228,692
Total noncurrent liabilities	<u>2,653,692</u>	<u>-</u>	<u>2,653,692</u>
TOTAL LIABILITIES	<u>3,237,939</u>	<u>12,318</u>	<u>3,250,257</u>
NET POSITION			
Investment in capital assets, net of related debt	3,226,372	74,047	3,300,419
Restricted	409,646	20,541	430,187
Unrestricted (deficit)	236,107	(17,015)	219,092
TOTAL NET POSITION	<u>\$ 3,872,125</u>	<u>\$ 77,573</u>	<u>\$ 3,949,698</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF ACTIVITIES
Year Ended June 30, 2013

<u>FUNCTIONS/PROGRAMS</u>	<u>Expenses</u>	<u>PROGRAM REVENUES</u>		
		<u>Charges for Services and Sales</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>
GOVERNMENTAL ACTIVITIES:				
Instruction	\$ 8,092,685	\$ 2,095	\$ 5,621,174	\$ -
Support services:				
Student	559,106	-	-	-
Instructional staff	844,499	-	-	-
District administration	617,461	-	-	-
School administration	840,264	-	-	-
Business	176,354	-	-	-
Plant operations and maintenance	1,229,864	-	-	-
Student transportation	574,612	-	-	-
Architectural/engineering	103,553	-	-	-
Community services activities	188,683	-	-	-
Interest on long-term debt	121,551	-	-	-
TOTAL GOVERNMENTAL ACTIVITIES	<u>\$13,348,632</u>	<u>\$ 2,095</u>	<u>\$ 5,621,174</u>	<u>\$ -</u>
BUSINESS-TYPE ACTIVITIES:				
Food service	\$ 1,080,933	\$ 124,567	\$ 973,282	\$ -
TOTAL BUSINESS-TYPE ACTIVITIES	<u>\$ 1,080,933</u>	<u>\$ 124,567</u>	<u>\$ 973,282</u>	<u>\$ -</u>
TOTAL PRIMARY GOVERNMENT	<u>\$14,429,565</u>	<u>\$ 126,662</u>	<u>\$ 6,594,456</u>	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

**NET (EXPENSES) REVENUES AND
CHANGES IN NET POSITION**

<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
\$ (2,469,416)		\$ (2,469,416)
(559,106)		(559,106)
(844,499)		(844,499)
(617,461)		(617,461)
(840,264)		(840,264)
(176,354)		(176,354)
(1,229,864)		(1,229,864)
(574,612)		(574,612)
(103,553)		(103,553)
(188,683)		(188,683)
<u>(121,551)</u>		<u>(121,551)</u>
<u>(7,725,363)</u>		<u>(7,725,363)</u>
	\$ 16,916	<u>16,916</u>
	<u>16,916</u>	<u>16,916</u>
		<u>(7,708,447)</u>

GENERAL REVENUES

Taxes			
Property	1,882,034	-	1,882,034
Motor vehicle	328,475	-	328,475
Utilities	693,972	-	693,972
State and formula grants	4,759,541	-	4,759,541
Earnings on investments	17,324	140	17,464
Compensation for loss of assets	1,207	-	1,207
Other local revenues	<u>133,166</u>	<u>-</u>	<u>133,166</u>
Total general revenues	7,815,719	140	7,815,859
Operating transfers (net)	<u>37,488</u>	<u>(37,488)</u>	<u>-</u>
Total general revenues and transfers	<u>7,853,207</u>	<u>(37,348)</u>	<u>7,815,859</u>
Change in net position	127,844	(20,432)	107,412
Net position, July 1, 2012	<u>3,744,281</u>	<u>98,005</u>	<u>3,842,286</u>
Net position, June 30, 2013	<u>\$ 3,872,125</u>	<u>\$ 77,573</u>	<u>\$ 3,949,698</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2013

	General Fund	Special Revenue	Other Governmental Funds	Total Governmental Funds
ASSETS AND RESOURCES				
Cash and cash equivalents	\$ 485,344	\$ (345,040)	\$ 93,485	\$ 233,789
Accounts receivable:				
Taxes – current	137,090	-	-	137,090
Accounts receivable	23,669	-	-	23,669
Intergovernmental – state	-	6,712	-	6,712
Intergovernmental – federal	8,963	514,047	-	523,010
Prepaid expenditures	3,577	-	-	3,577
TOTAL ASSETS AND RESOURCES	<u>\$ 658,643</u>	<u>\$ 175,719</u>	<u>\$ 93,485</u>	<u>\$ 927,847</u>
LIABILITIES				
Accounts payable	\$ 104,800	\$ 9,965	\$ -	\$ 114,765
Accrued salaries and benefits payable	1,575	19,447	-	21,022
Deferred revenue	-	146,307	-	146,307
TOTAL LIABILITIES	<u>106,375</u>	<u>175,719</u>	<u>-</u>	<u>282,094</u>
FUND BALANCES				
Unassigned	275,729	(39,622)	-	236,107
Restricted				
Sick leave payable	54,250	-	-	54,250
Future construction projects	-	-	10	10
Debt service	-	-	93,475	93,475
Assigned				
Purchase obligations	30,494	39,622	-	70,116
Site based carryforward	191,795	-	-	191,795
TOTAL FUND BALANCES	<u>552,268</u>	<u>-</u>	<u>93,485</u>	<u>645,753</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 658,643</u>	<u>\$ 175,719</u>	<u>\$ 93,485</u>	<u>\$ 927,847</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

RECONCILIATION OF THE BALANCE SHEET – GOVERNMENTAL FUNDS TO THE
STATEMENT OF NET POSITION
June 30, 2013

Total Fund Balances per fund financial statements		\$ 645,753
Amounts reported for governmental activities in the statement of net position are different because:		
Capital assets used in governmental activities are not financial resources, but they are reported in the statement of net position		6,182,217
Certain liabilities, such as bonds payable and lease obligations, are not reported in this fund financial statement because they are not due and payable in the current period, but they are presented in the statement of net position:		
Bonds payable	\$ (2,670,000)	
Lease obligations	<u>(285,845)</u>	<u>(2,955,845)</u>
Total Net Position for Governmental Activities		<u>\$ 3,872,125</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
Year Ended June 30, 2013

	<u>General Fund</u>	<u>Special Revenue</u>
REVENUES		
From local sources:		
Taxes		
Property	\$ 1,659,140	\$ -
Motor vehicle	328,475	-
Utilities	693,972	-
Tuition and fees	2,095	-
Earnings on investments	17,041	283
Other local revenues	60,794	72,372
Intergovernmental – state	7,582,831	529,877
Intergovernmental – indirect federal	-	1,725,779
Intergovernmental – direct federal	44,338	66,856
TOTAL REVENUES	<u>10,388,686</u>	<u>2,395,167</u>
EXPENDITURES		
Instruction	5,800,707	1,963,014
Support services:		
Student	489,727	44,781
Instructional staff	650,954	193,221
District administration	561,914	5,701
School administration	830,476	4,891
Business	157,638	18,716
Plant operations and maintenance	1,223,917	-
Student transportation	487,861	17,909
Architectural/engineering	103,553	-
Community services activities	10,226	176,192
Payment of bonds/debt service	-	-
Payment of lease obligations	37,315	-
Payment of interest	-	-
TOTAL EXPENDITURES	<u>10,354,288</u>	<u>2,424,425</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>34,398</u>	<u>(29,258)</u>
OTHER FINANCING SOURCES (USES)		
Compensation for loss of assets	1,207	-
Operating transfers in	37,488	29,258
Operating transfers out	(29,258)	-
TOTAL OTHER FINANCING SOURCES (USES)	<u>9,437</u>	<u>29,258</u>
NET CHANGES IN FUND BALANCES	43,835	-
FUND BALANCES, JULY 1, 2012	<u>508,433</u>	<u>-</u>
FUND BALANCES, JUNE 30, 2013	<u>\$ 552,268</u>	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

Other Governmental Funds	Total Governmental Funds
\$ 222,894	\$ 1,882,034
-	328,475
-	693,972
-	2,095
-	17,324
-	133,166
431,034	8,543,742
-	1,725,779
-	111,194
<u>653,928</u>	<u>13,437,781</u>
-	7,763,721
-	534,508
-	844,175
73,604	641,219
-	835,367
-	176,354
-	1,223,917
-	505,770
-	103,553
-	186,418
530,000	530,000
-	37,315
<u>121,551</u>	<u>121,551</u>
<u>725,155</u>	<u>13,503,868</u>
<u>(71,227)</u>	<u>(66,087)</u>
-	1,207
625,735	692,481
<u>(625,735)</u>	<u>(654,993)</u>
-	<u>38,695</u>
(71,227)	(27,392)
<u>164,712</u>	<u>673,145</u>
<u>\$ 93,485</u>	<u>\$ 645,753</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
Year Ended June 30, 2013

Total Net Change In Fund Balances – per fund financial statements	\$ (27,392)
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Amounts reported for governmental activities in the statement of activities
are different because:

Governmental funds report capital outlays as expenditures. However, in the
statement of activities, the cost of those assets is allocated over their
estimated useful lives as depreciation expense.

Depreciation	\$ (531,598)	
Capital outlays	<u>271,202</u>	(260,396)

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces noncurrent liabilities in the statement of net position and does not result in an expense in the statement of activities.	530,000
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Payments on lease obligations are an expenditure in the governmental funds, but the payments reduce noncurrent lease obligations in the statement of net position and do not result in an expense in the statement of activities.	38,277
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Proceeds from lease obligations used to purchase capital assets reduce expenditures in the governmental funds, but the proceeds increase lease obligations in the statement of net position.	<u>(152,645)</u>
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Change In Net Position of Governmental Activities	<u>\$ 127,844</u>
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The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE – BUDGET AND ACTUAL
GENERAL FUND
Year Ended June 30, 2013

	Budgeted Amounts	
	<u>Original</u>	<u>Final</u>
REVENUES		
From local sources:		
Taxes		
Property	\$ 1,608,000	\$ 1,608,000
Motor vehicle	230,000	230,000
Utilities	640,000	640,000
Revenue in lieu of taxes – state and local	22,000	22,000
Tuition and fees	3,100	3,100
Earnings on investments	20,000	20,000
Other local revenues	77,700	77,700
Intergovernmental – state	5,738,043	5,738,043
Intergovernmental – direct federal	32,000	32,000
TOTAL REVENUES	<u>8,370,843</u>	<u>8,370,843</u>
EXPENDITURES		
Instruction	4,600,171	4,600,171
Support services:		
Student	405,474	405,474
Instructional staff	537,186	537,186
District administration	437,058	437,058
School administration	764,388	764,388
Business	138,824	138,824
Plant operations and maintenance	1,086,942	1,086,942
Student transportation	450,894	450,894
Architectural/engineering	89,979	89,979
Community services activities	8,194	8,194
Payment of lease obligations	37,315	37,315
Contingency	274,042	274,042
TOTAL EXPENDITURES	<u>8,830,467</u>	<u>8,830,467</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(459,624)</u>	<u>(459,624)</u>
OTHER FINANCING SOURCES (USES)		
Compensation for loss of assets	-	-
Operating transfers in	35,000	35,000
Operating transfers out	(25,000)	(25,000)
TOTAL OTHER FINANCING SOURCES (USES)	<u>10,000</u>	<u>10,000</u>
NET CHANGE IN FUND BALANCE	(449,624)	(449,624)
FUND BALANCE, JULY 1, 2012	<u>449,624</u>	<u>449,624</u>
FUND BALANCE, JUNE 30, 2013	<u>\$ -</u>	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

<u>Actual</u>	<u>Variance with Final Budget Favorable or (Unfavorable)</u>
\$ 1,659,140	\$ 51,140
328,475	98,475
693,972	53,972
-	(22,000)
2,095	(1,005)
17,041	(2,959)
60,794	(16,906)
7,582,831	1,844,788
44,338	12,338
<u>10,388,686</u>	<u>2,017,843</u>
5,800,707	(1,200,536)
489,727	(84,253)
650,954	(113,768)
561,914	(124,856)
830,476	(66,088)
157,638	(18,814)
1,223,917	(136,975)
487,861	(36,967)
103,553	(13,574)
10,226	(2,032)
37,315	-
-	274,042
<u>10,354,288</u>	<u>(1,523,821)</u>
<u>34,398</u>	<u>494,022</u>
1,207	1,207
37,488	2,488
(29,258)	(4,258)
<u>9,437</u>	<u>(563)</u>
43,835	493,459
<u>508,433</u>	<u>58,809</u>
<u>\$ 552,268</u>	<u>\$ 552,268</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE – BUDGET AND ACTUAL
SPECIAL REVENUE FUND
Year Ended June 30, 2013

	Budgeted Amounts			Variance with Final Budget Favorable or (Unfavorable)
	<u>Original</u>	<u>Final</u>	<u>Actual</u>	
REVENUES				
From local sources:				
Taxes				
Property	\$ -	\$ -	\$ -	\$ -
Motor vehicle	-	-	-	-
Utilities	-	-	-	-
Revenue in lieu of taxes – state and local	-	-	-	-
Tuition and fees	-	-	-	-
Earnings on investments	100	100	283	183
Other local revenues	53,000	58,000	72,372	14,372
Intergovernmental – state	532,862	559,417	529,877	(29,540)
Intergovernmental – federal	1,727,967	1,817,103	1,792,635	(24,468)
TOTAL REVENUES	<u>2,313,929</u>	<u>2,434,620</u>	<u>2,395,167</u>	<u>(39,453)</u>
EXPENDITURES				
Instruction	1,843,275	1,987,746	1,963,014	24,732
Support services:				
Student	34,792	35,416	44,781	(9,365)
Instructional staff	226,135	167,109	193,221	(26,112)
District administration	9,645	14,524	5,701	8,823
School administration	2,908	2,908	4,891	(1,983)
Business	17,854	19,324	18,716	608
Plant operations and maintenance	-	25,000	-	25,000
Student transportation	17,037	21,037	17,909	3,128
Community services activities	187,283	186,556	176,192	10,364
TOTAL EXPENDITURES	<u>2,338,929</u>	<u>2,459,620</u>	<u>2,424,425</u>	<u>35,195</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(25,000)	(25,000)	(29,258)	(4,258)
OTHER FINANCING SOURCES (USES)				
Operating transfers in	25,000	25,000	29,258	4,258
NET CHANGE IN FUND BALANCE	-	-	-	-
FUND BALANCE, JULY 1, 2012	-	-	-	-
FUND BALANCE, JUNE 30, 2013	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF NET POSITION
PROPRIETARY FUND
June 30, 2013

	<u>ASSETS</u>	<u>Food Service</u>
CURRENT ASSETS		
Cash and cash equivalents		\$ (103,557)
Accounts receivable:		
Accounts receivable		2,917
Intergovernmental – federal		101,691
Materials and supplies inventory		<u>14,793</u>
Total current assets		<u>15,844</u>
NONCURRENT ASSETS		
Capital assets, net		<u>74,047</u>
TOTAL ASSETS		<u>89,891</u>
	<u>LIABILITIES AND NET POSITION</u>	
CURRENT LIABILITIES		
Accounts payable		8,069
Accrued salaries and benefits payable		<u>4,249</u>
TOTAL CURRENT LIABILITIES		<u>12,318</u>
NET POSITION		
Investment in capital assets		74,047
Unrestricted (deficit)		(17,015)
Restricted		
Sick leave payable		5,748
Nonspendable – inventories		<u>14,793</u>
TOTAL NET POSITION		<u>\$ 77,573</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
PROPRIETARY FUND
Year Ended June 30, 2013

	<u>Food Service</u>
OPERATING REVENUES	
Sales	\$ 124,567
TOTAL OPERATING REVENUES	<u>124,567</u>
OPERATING EXPENSES	
Salaries	346,640
Employee benefits	155,850
Purchased services	9,928
Supplies and materials	557,744
Depreciation	10,771
Operating transfers	37,488
TOTAL OPERATING EXPENSES	<u>1,118,421</u>
OPERATING INCOME (LOSS)	<u>(993,854)</u>
NON-OPERATING REVENUES (EXPENSES)	
Operating grants-federal	844,983
Operating grants-state	74,580
Child nutrition program – donated commodities	46,719
Local grants	7,000
Earnings on investments	140
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>973,422</u>
CHANGE IN NET POSITION	(20,432)
NET POSITION, JULY 1, 2012	<u>98,005</u>
NET POSITION, JUNE 30, 2013	<u>\$ 77,573</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF CASH FLOWS
PROPRIETARY FUND
Year Ended June 30, 2013

	<u>Food Service</u>
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from sales	\$ 125,056
Cash payments for salaries	(348,152)
Cash payments for employee benefits	(155,850)
Cash payments for purchased services	(9,928)
Cash payments for supplies and materials	(556,161)
Cash payments for other operating expenses	<u>(37,488)</u>
Net cash provided (used) by operating activities	<u>(982,523)</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Receipt of interest	140
Receipt of grants	842,034
Receipt of donated commodities	<u>46,719</u>
Net cash provided (used) by investing activities	<u>888,893</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(93,630)
CASH AND CASH EQUIVALENTS, JULY 1, 2012	<u>(9,927)</u>
CASH AND CASH EQUIVALENTS, JUNE 30, 2013	<u>\$ (103,557)</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	
Operating income (loss)	\$ (993,854)
ADJUSTMENTS TO RECONCILE OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	
Depreciation	10,771
Changes in assets and liabilities:	
Accounts receivable	489
Accounts payable	1,583
Accrued salaries and benefits payable	<u>(1,512)</u>
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>\$ (982,523)</u>
SCHEDULE OF NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES	
Donated commodities received from federal government	<u>\$ 46,719</u>
On-behalf payments from state government	<u>\$ 66,483</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF FIDUCIARY NET POSITION
June 30, 2013

	SCHOOL ACTIVITY FUNDS
<u>ASSETS</u>	
CURRENT ASSETS	
Cash and cash equivalents	\$ 99,299
Accounts receivable	<u>1,995</u>
TOTAL ASSETS	<u>101,294</u>
<u>LIABILITIES AND NET POSITION</u>	
CURRENT LIABILITIES	
Accounts payable	1,378
Due to students	<u>99,916</u>
TOTAL LIABILITIES	<u>101,294</u>
NET POSITION	<u>\$ -</u>

The accompanying notes are an integral part of these financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies that affect the significant elements of the Middlesboro Independent School District are summarized as follows:

REPORTING ENTITY

The Middlesboro Independent Board of Education (Board), a five-member group, is the level of government which has oversight responsibilities over all activities related to public elementary and secondary school education within the jurisdiction of the Middlesboro Independent School District (District). The District receives funding from local, state and federal government sources and must comply with the commitment requirements of these funding source entities. However, the District is not included in any other governmental "reporting entity" as defined by the Governmental Accounting Standards Board (GASB) pronouncement since Board members are elected by the public and have decision making authority, the power to designate management, the responsibility to develop policies which may influence operations and primary accountability for fiscal matters.

The District, for financial purposes, includes all of the funds and account groups relevant to the operation of the Middlesboro Independent School District. The financial statements presented herein do not include funds of groups and organizations, which although associated with the school system, have not originated within the District itself such as Band Boosters, Parent-Teacher Associations, etc.

The financial statements of the District include those of separately administered organizations that are controlled by or dependent on the District. Control or dependence is determined on the basis of budget adoption, funding and appointment of the respective governing board.

Based on the foregoing criteria, the financial statement of the following organization is included in the accompanying financial statements:

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT FINANCE CORPORATION

The Middlesboro Independent Board of Education resolved to authorize the establishment of the Middlesboro Independent School District Finance Corporation (a non-profit, non-stock, public and charitable corporation organized under the School Board Act and KRS 273 and KRS Section 58.180) as an agency of the District for financing the costs of school building facilities. The Board members of the Middlesboro Independent Board of Education also comprise the corporation's Board of Directors.

BASIS OF PRESENTATION

Government-Wide Financial Statements: The statement of net position and the statement of activities display information about the District as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. The statements distinguish between governmental and business-type activities of the District.

The government-wide financial statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements of governmental funds.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the District and for each function or program of the governmental activities of the District. Direct expenses are those that are specifically associated with a service,

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

program or department and therefore clearly identifiable to a particular function. Program revenues include amounts paid by the recipient of goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. All taxes and revenues not classified as program revenues are presented as general revenues of the District, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each business segment or governmental function is self-financing or draws from the general revenues of the District.

Fund Financial Statements: Fund financial statements report detailed information about the District. Their focus is on major funds rather than reporting funds by type. Each major fund is presented in a separate column, and all nonmajor funds are aggregated into one column. Fiduciary funds are reported by fund type.

The accounting and reporting treatment applied to a fund is determined by its measurement focus. All governmental fund types are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations of these funds are included on the balance sheet. Proprietary fund's operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total position.

The District has the following funds:

I. Governmental Fund Types

- (A) The General Fund is the main operating fund of the District. It accounts for financial resources used for general types of operations. This is a budgeted fund, and any fund balances are considered as resources available for use. This is a major fund of the District.
- (B) The Special Revenue (Grant) Funds account for proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to disbursements for specified purposes. It includes federal financial programs where unused balances are returned to the grantor at the close of the specified project periods as well as the state grant programs. Project accounting is employed to maintain integrity for the various sources of funds. The separate projects of federally funded grant programs are identified in the Schedule of Expenditures of Federal Awards included in this report on pages 40 through 42. This is a major fund of the District.
- (C) Capital Project Funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities and equipment (other than those financed by the Proprietary Fund):
 - 1. The Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund receives those funds designated by the state as Capital Outlay funds and is restricted primarily for use in financing projects identified in the District's facility plan.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. The Facility Support Program of Kentucky (FSPK) accounts for funds generated by the building tax levy required to participate in the School Facilities Construction Commission's construction funding and state matching funds, where applicable. Funds may be used for projects identified in the District's facility plan.
3. The Construction Fund accounts for proceeds from sales of bonds and other revenues to be used for authorized construction.

(D) Debt Service Funds

The Debt Service Funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest and related costs; and for the payment of interest on general obligation notes payable, as required by Kentucky Law.

II. Proprietary Fund Types (Enterprise Funds)

- (A) The Food Service Fund is used to account for school food service activities, including the National School Lunch Program, which is conducted in cooperation with the U.S. Department of Agriculture (USDA). Amounts have been recorded for in-kind contributions of commodities from the USDA. The Food Service Fund is a major fund.

The District applies all GASB pronouncements to proprietary funds as well as the Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

III. Fiduciary Fund Type (Agency Funds)

- (A) The School Activity Funds account for activities of student groups and other types of activities requiring clearing accounts. These funds are accounted for in accordance with the Uniform Program of Accounting for School Activity Funds.

BASIS OF ACCOUNTING

Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. The fund financial statements are prepared using either modified accrual for governmental funds or accrual basis for proprietary and fiduciary funds.

Revenues, Exchange and Nonexchange Transactions: Revenues resulting from exchange transactions, in which each party receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenues are recognized in the fiscal year when they become both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current fiscal year. The available period of the District is sixty days after year end.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Nonexchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been met. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the District must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. On the modified accrual basis, revenue from nonexchange transactions must also be available before it can be recognized.

Deferred Revenue: The District reports deferred revenue on its statement of net position and governmental funds balance sheet. In both the government-wide and governmental fund statements, grants that are intended to finance future periods are reported as deferred revenue. In subsequent periods, the liability for deferred revenue is removed from the statement of net position and governmental funds balance sheet and revenue is recognized.

Expenditures/Expenses: On the accrual basis of accounting, expenses are recorded at the time they are incurred. The measurement focus of governmental fund accounting is on flow of current financial resources. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred except for (1) principal and interest on general long-term debt, which is recorded when due, and (2) the costs of accumulated unpaid vacation and sick leave, which are reported as fund liabilities in the period in which they will be liquidated with available financial resources rather than in the period earned by employees.

CASH AND INVESTMENTS

The District maintains a cash and investment pool used by all funds. The cash and investment pool has the same characteristics as demand deposits. Each fund type's portion of this pool is displayed in the financial statements as cash and cash equivalents in that fund. The District utilizes a financial institution to service bonded debt as principal and interest payments come due. The monies are either maintained in a central bank account or used to purchase legal investments.

It is the policy of the District to value investment contracts and money market investments with a maturity of one year or less at the time of purchase at cost or amortized cost. Investment contracts and money market investments that had a remaining maturity of greater than one year at the time of purchase are reported at fair value.

The Kentucky Revised Statutes authorized the District to invest in United States and State of Kentucky bonds, notes and other obligations; bank certificates of deposit; bankers' acceptances; and commercial paper notes rated prime and issued by United States corporations. It is the District's policy to invest in all of the above types of investments. Under existing Kentucky statutes, all investment earnings accrue to the general and food service funds except certain trust funds and those funds individually authorized by Board resolution.

PREPAID ASSETS/EXPENDITURES

Payments made that will benefit periods beyond June 30, 2013 are recorded as prepaid items using the consumption method. A current asset for the prepaid amount is recorded at the time of the purchase and an expenditure/expense is reported in the year in which services are consumed.

INVENTORY

On government-wide financial statements, inventories are presented at cost or using the first in, first out (FIFO) method and are expensed when used.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

On fund financial statements, inventories are valued at cost while inventories of proprietary funds are stated at lower of cost or market. For all funds, cost is determined using the FIFO method, and are determined by physical count. Inventory in governmental funds consists of expendable supplies held for consumption. The cost is recorded as an expenditure at the time of purchase. Reported inventories in these funds are equally offset by a fund balance reserve, which indicates they do not represent available spendable resources. Inventories of proprietary funds consist of donated and purchased food.

CAPITAL ASSETS AND DEPRECIATION

General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets are reported in the government-wide statement of net position but are not reported in the fund financial statements. Capital assets utilized by proprietary funds are reported on both statement types.

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. The District follows the policy of not capitalizing assets with a cost of less than \$1,000 with the exception of assets acquired with Technology Funds, which there is no threshold, and a useful life of less than 1 year. The District does not possess any infrastructure.

All reported capital assets, with the exception of land, are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives for both governmental fund capital assets and proprietary fund capital assets:

<u>Description</u>	<u>Useful Life</u>
Land improvements	20 years
Buildings and improvements	25-50 years
Technology equipment	5 years
Vehicles	5-10 years
Food service equipment	10-12 years
General equipment	7 years

INTERFUND ACTIVITY

Transfers between governmental and business-type activities on the government-wide statements are reported in the same manner as general revenues. Sales of goods and services between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds and as operating expenses in proprietary funds.

On fund financial statements, short-term interfund loans are classified as interfund receivables/payables. These amounts are eliminated in the statement of net position, except for amounts due between governmental and business-type activities, which are presented as internal balances.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ACCUMULATED UNPAID SICK LEAVE BENEFITS

Vacation benefits are accrued as a liability as the benefits are earned if the employee's right to receive compensation is attributable to services already rendered and it is probable that the employer will compensate the employees for the benefits through paid time off or some other means. Sick leave benefits are accrued as a reservation of fund balance using the vesting method. The amount is based on the sick leave accumulated at June 30 by those employees who are currently eligible to receive termination payments and those employees for whom it is probable they will become eligible to receive termination benefits in the future. The criteria for determining the vacation and sick leave liability is derived from Board policy, negotiated agreements, and state laws.

The entire compensated absences reservation is reported on the government-wide financial statements. For governmental fund financial statements, the amount of accumulated vacation and sick leave of employees has been recorded as a reservation to the extent that the amounts are expected to be paid using expendable available financial resources. For proprietary funds, the entire amount of compensated absences is recorded as an expense and liability of the fund.

ON-BEHALF PAYMENTS FOR FRINGE BENEFITS

The District recognizes as revenues and expenses contributions made by the State of Kentucky for health insurance and flexible spending accounts on behalf of the District's employees. In fiscal year 2013, the State made contributions of \$1,976,593, consisting of \$1,910,110 for governmental funds and \$66,483 for the proprietary fund.

ACCRUED LIABILITIES AND LONG-TERM DEBT

All accrued liabilities and long-term debt are reported in the government-wide financial statements as well as the proprietary fund financial statements.

For governmental fund financial statements, the accrued liabilities are generally reported as a governmental fund liability if due for payment as of the balance sheet date regardless of whether they will be liquidated with current financial resources. However, claims and judgments and compensated absences paid from governmental funds are reported as a liability in the fund financial statements only for the portion expected to be financed from expendable available financial resources. Long-term debt paid from governmental funds is not recognized as a liability in the fund financial statements until due.

RESTRICTED RESOURCES

The District applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted assets are available.

NET POSITION

Net position in government-wide and proprietary fund financial statements are classified as invested in capital assets, net of related debt; restricted; and unrestricted. Restricted net assets represent constraints on resources that are either a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or b) imposed by law through state statute.

In the governmental fund financial statements, fund balance is composed of five classifications designed to disclose the hierarchy of constraint placed on how fund balance can be spent.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The governmental fund types classify fund balances as follows:

Nonspendable Fund Balance – This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

- *Inventories* – Portion of fund balance that is not an available resource because it represents the year-end balance of ending inventories, which are not spendable resources.

Restricted Fund Balance – This classification includes revenue sources that are restricted to specific purposes externally imposed by creditors, grantors or imposed by law.

Committed Fund Balance – Portion of fund balance that can only be used for specific purposes imposed by a majority vote of the Middlesboro Independent School District's Board members. Any changes or removal of specific purposes also requires majority action by the Board.

Assigned Fund Balance – Portion of fund balance that has been budgeted by the Board.

- *Purchase Obligations* – Portion of fund balance that is appropriated in the subsequent year's budget that is not already classified in restricted or committed.
- *Site Base* – Portion of fund balance that has been budgeted for future site base expenditures.

Unassigned Fund Balance – Portion of fund balance that has not been restricted, committed or assigned for a specific purpose.

OPERATING REVENUES AND EXPENSES

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the District, those revenues are primarily charges for meals provided by the various schools.

CONTRIBUTIONS OF CAPITAL

Contributions of capital in proprietary fund financial statements arise from outside contributions of fixed assets, or from grants or outside contributions of resources restricted to capital acquisition and construction.

ESTIMATES

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires the District's management to make estimates and assumptions that affect reported amounts of assets, liabilities, fund balances, and disclosure of contingent assets and liabilities at the date of the basic financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

BUDGETARY PROCESS

Budgetary Basis of Accounting: The District's budgetary process accounts for certain transactions on a basis other than U.S. Generally Accepted Accounting Principles (GAAP). The major differences between the budgetary basis and the GAAP basis are:

Revenues are recorded when received in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Expenditures are recorded when paid in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

Once the budget is approved, it can be amended. Amendments are presented to the Board at their regular meetings. Per Board policy, only amendments that aggregate greater than \$50,000 require Board approval. Such amendments are made before the fact, are reflected in the official minutes of the Board, and are not after fiscal year end as dictated by law.

Each budget is prepared and controlled by the budget coordinator at the revenue and expenditure function/object level. All unencumbered budget appropriations lapse at year-end.

NOTE 2 – CASH AND CASH EQUIVALENTS

The District's funds are required to be deposited and invested under the terms of a depository contract pursuant to the School Depository Act. The depository bank deposits for safekeeping and trust with the District's third party agent approved pledged securities in an amount sufficient to protect District funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the dollar amount of Federal Deposit Insurance Corporation insurance.

Under the depository contract, the District, at its own discretion, invests funds in time deposits and certificates of deposit provided by the depository bank at interest rates approximating United States Treasury Bill rates.

At June 30, 2013, the carrying amount of the District's deposits was \$130,232 and the bank balance was \$1,323,396. The entire bank balance throughout the year was covered by federal depository insurance or by collateral held by the District's agent in the District's name.

The deposits were deemed collateralized under Kentucky Law during the year and the District maintains copies of all safekeeping receipts. The following is disclosed:

- a. Name of banks utilized during fiscal year: Community Trust Bank and First State Bank.
- b. Amount of bond and/or security pledged as of the date of the highest combined balance on deposit was \$1,979,702.
- c. Largest cash, savings and time deposit combined account balance amounted to \$2,121,262 and occurred during the month of June.
- d. Total amount of FDIC coverage at the time of largest combined balance was \$250,000 per bank.

The cash deposits held at financial institutions can be categorized according to three levels of risk.

These three levels of risk are as follows:

- | | |
|------------|---|
| Category 1 | Deposits, which are insured or collateralized with securities, held by the District or by its agent in the District's name. |
|------------|---|

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

Category 2 Deposits, which are collateralized with securities held by the pledging financial institution's trust department or agent in the District's name.

Category 3 Deposits, which are not collateralized or insured.

Based on these three levels of risk, all of the District's cash deposits are classified as Category 1 and 2.

NOTE 3 – PROPERTY TAXES

The District's ad valorem property tax is levied each October 1 on the assessed value listed as of the prior January 1 for all real and business personal property located in the District. The assessed value of the certified roll, upon which the levy for the 2013 fiscal year was based, was \$408,482,356. The tax rates assessed for the year ended June 30, 2013 to finance general fund operations were \$.485 per \$100 valuation for real estate, \$.485 for tangible property and \$.56 for motor vehicles. The District committed \$.058 of the levy to the FSPK Fund. Taxes are due on December 31, and become delinquent by February 1 following the October 1 levy date. Current tax collections for the year ended June 30, 2013 were ninety-two percent of the tax levies. Delinquent taxes are allocated to the general fund. The District records taxes receivable only for the amounts collected during the next sixty days from its fiscal year end.

The District levies a utility gross receipts license tax in the amount of 3% of the gross receipts derived from the furnishings, within the county, of telephonic and telegraphic communications services, cablevision services, electric power, water, and natural, artificial and mixed gas.

At June 30, 2013, the components of taxes receivable were as follows:

Motor vehicle tax	\$ 12,800
General property tax	668
PSC property tax	65,164
Delinquent property tax	2,880
Penalties and interest on taxes	1,529
Utilities tax	54,049
	<u>\$ 137,090</u>

NOTE 4 – RECEIVABLES

Receivables at June 30, 2013 consisted of taxes, accounts (rent and student fees), interest and intergovernmental grants and entitlements. All receivables are considered collectible in full due to the ability to foreclose for the nonpayment of taxes, the stable condition of State programs and the current year guarantee of federal funds.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 5 – CAPITAL ASSETS

A summary of capital assets activity during the fiscal year follows:

	Balance July 1, 2012	Additions	Deletions	Balance June 30, 2013
GOVERNMENTAL ACTIVITIES				
Land	\$ 177,607	\$ -	\$ -	\$ 177,607
Land improvements	655,236	-	-	655,236
Buildings and improvements	12,437,023	-	-	12,437,023
Technology equipment	1,573,104	111,906	-	1,685,010
Vehicles	1,154,025	132,634	-	1,286,659
General equipment	675,996	26,662	-	702,658
Totals at cost	<u>16,672,991</u>	<u>271,202</u>	<u>-</u>	<u>16,944,193</u>
Less accumulated depreciation:				
Land improvements	533,716	24,418	-	558,134
Buildings and improvements	6,861,166	323,915	-	7,185,081
Technology equipment	1,316,895	93,663	-	1,410,558
Vehicles	965,968	48,831	-	1,014,799
General equipment	552,633	40,771	-	593,404
Total accumulated depreciation	<u>10,230,378</u>	<u>531,598</u>	<u>-</u>	<u>10,761,976</u>
Governmental activities capital assets, net	<u>\$ 6,442,613</u>	<u>\$ (260,396)</u>	<u>\$ -</u>	<u>\$ 6,182,217</u>
BUSINESS-TYPE ACTIVITIES				
Food service equipment	\$ 245,560	\$ -	\$ -	\$ 245,560
Technology equipment	24,613	-	-	24,613
Vehicles	8,650	-	-	8,650
Totals at cost	<u>278,823</u>	<u>-</u>	<u>-</u>	<u>278,823</u>
Less accumulated depreciation:				
Food service equipment	162,779	10,282	-	173,061
Technology equipment	22,576	489	-	23,065
Vehicles	8,650	-	-	8,650
Total accumulated depreciation	<u>194,005</u>	<u>10,771</u>	<u>-</u>	<u>204,776</u>
Business-type activities capital assets, net	<u>\$ 84,818</u>	<u>\$ (10,771)</u>	<u>\$ -</u>	<u>\$ 74,047</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 5 – CAPITAL ASSETS (CONTINUED)

Depreciation expense was allocated to governmental functions as follows:

Instruction	\$ 441,832
Support services:	
Student	24,598
Instructional staff	324
District administration	2,904
School administration	4,897
Plant operations and maintenance	5,947
Student transportation	48,831
Community services activities	2,265
Total governmental activities	<u>\$ 531,598</u>

NOTE 6 – BONDED DEBT AND LEASE OBLIGATIONS

The original amount of each bond issue, the issue date, and interest rates are summarized as follows:

<u>Issue</u>	<u>Original</u>	<u>Interest</u>
	<u>Amount</u>	<u>Rates</u>
2004	\$ 475,000	4.75%
2005	765,000	3.25% to 3.6%
2006	1,965,000	3.9% to 4.4%

The District, through the General Fund (including utility taxes and the Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund), is obligated to make lease payments in amounts sufficient to satisfy debt service requirements on bonds issued by the Middlesboro Independent School District and the Middlesboro Independent School District Finance Corporation to construct school facilities. The District has an option to purchase the property under lease at any time by retiring the bonds then outstanding.

In 1990, the District entered into "participation agreements" with the Kentucky School Facility Construction Commission. The Commission was created by the Kentucky Legislature for the purpose of assisting local school districts in meeting school construction needs. The table below sets forth the amount to be paid by the District and the Commission for each year until maturity of all bond issues.

The bonds may be called prior to maturity and redemption premiums are specified in each issue. Assuming no bonds are called prior to scheduled maturity, the minimum obligations of the District, including amounts to be paid by the Commission, at June 30, 2013 for debt service (principal and interest) are as follows:

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 6 – BONDED DEBT AND LEASE OBLIGATIONS (CONTINUED)

<u>Year</u>	<u>Middlesboro Independent School District</u>		<u>Kentucky School Facility Construction Commission</u>		<u>Total</u>
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	
2013-14	\$ 184,520	\$ 76,859	\$ 60,480	\$ 29,673	\$ 351,532
2014-15	192,157	70,035	62,843	27,309	352,344
2015-16	199,529	62,775	65,471	24,681	352,456
2016-17	204,913	55,136	60,087	22,063	342,199
2017-18	93,859	49,284	46,141	19,760	209,044
2018-19	101,854	45,210	48,146	17,756	212,966
2019-20	104,621	40,874	50,379	15,522	211,396
2020-21	112,287	36,291	52,713	13,186	214,477
2021-22	119,951	31,355	55,049	10,853	217,208
2022-23	122,378	26,175	57,622	8,277	214,452
2023-24	124,684	20,864	60,316	5,584	211,448
2024-25	132,107	15,276	27,893	2,764	178,040
2025-26	137,493	9,345	27,507	1,545	175,890
2026-27	143,646	3,160	21,354	470	168,630
	<u>\$ 1,973,999</u>	<u>\$ 542,639</u>	<u>\$ 696,001</u>	<u>\$ 199,443</u>	<u>\$ 3,412,082</u>

The District has purchased five buses through KISTA. The original amount of each lease obligation, lease date, and purpose are summarized as follows:

<u>Lease</u>	<u>Original Amount</u>	<u>Purpose</u>
Series 2006 (1)	\$ 80,233	KISTA – Bus purchase
Series 2006 (2)	80,396	KISTA – Bus purchase
Series 2008	72,693	KISTA – Bus purchase
Series 2009	77,265	KISTA – Bus purchase
Series 2013	104,420	KISTA – Bus purchase

Principal payments in the amount of \$31,205 were paid during the fiscal year.

The minimum obligations at June 30, 2013 for these lease obligations are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013-14	\$ 43,712	\$ 7,154	\$ 50,866
2014-15	43,485	5,808	49,293
2015-16	41,403	4,447	45,850
2016-17	33,282	3,097	36,379
2017-18	24,451	2,040	26,491
2018-19	17,910	1,307	19,217
2019-20	10,742	809	11,551
2020-21	11,001	594	11,595
2021-22	9,260	374	9,634
2022-23	9,446	189	9,635
	<u>\$ 244,692</u>	<u>\$ 25,819</u>	<u>\$ 270,511</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 6 – BONDED DEBT AND LEASE OBLIGATIONS (CONTINUED)

The District entered into a lease agreement with Kubota Leasing in the amount of \$18,395 for the purchase of a tractor/loader/backhoe and a 60" mower. Interest is being charged at 8.641%. Principal payments in the amount of \$3,576 were paid during the fiscal year.

The District entered into two different lease agreements with GMAC/ALLY for vehicles. One lease was for \$15,098 for the purchase of a 2011 Chevrolet Impala. Interest on this lease is 7.34%. Principal payments in the amount of \$1,722 were paid during the fiscal year. The second lease was for the purchase of a 2007 Chevrolet Uplander Van. Interest on this lease was 8.94%. Principal payments in the amount of \$1,774 were paid during the fiscal year.

The minimum obligations at June 30, 2013 for these lease obligations are as follows:

Year	Principal	Interest	Total
2013-14	\$ 13,441	\$ 2,907	\$ 16,348
2014-15	10,378	1,782	12,160
2015-16	5,077	1,223	6,300
2016-17	5,506	794	6,300
2017-18	5,972	328	6,300
2018-19	779	6	785
	<u>\$ 41,153</u>	<u>\$ 7,040</u>	<u>\$ 48,193</u>

The assets under capital lease are being depreciated. This depreciation is included in total depreciation expense and is allocated to governmental functions.

NOTE 7 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To obtain insurance for workers' compensation, errors and omissions and general liability coverage, the District participated in the Kentucky School Boards Insurance Trust Liability Insurance Fund. These public entity risk pools operate as common risk management and insurance programs for all school districts and other tax supported educational agencies of Kentucky who are members of the Kentucky School Boards Association. The District paid an annual premium to each fund for coverage. Contributions to the workers' compensation fund were based on premium rates established by such funds in conjunction with the excess insurance carrier, subject to claims experience modifications and a group discount amount. Dividends may be declared, but are not payable until twenty-four months after the expiration of the self-insurance term. The liability insurance fund pays insurance premiums of the participating members established by the insurance carrier. The Trust can terminate coverage if it is unable to obtain acceptable excess general liability coverage and for any reason by giving ninety (90) days notice. In the event the Trust terminated coverage, any amount remaining in the Fund (after payment of operational and administrative costs and claims for which coverage was provided) would be returned to the member on a pro-rata basis.

The District purchased unemployment insurance through the Kentucky School Boards Insurance Trust Unemployment Compensation Fund, however, risk has not been transferred to such fund. In addition, the District continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 7 – RISK MANAGEMENT (CONTINUED)

The District has been notified by the Kentucky School Boards Insurance Trust (KSBIT) of a liability assessment that will be due in the near term. The preliminary estimated liability assessment provided by KSBIT indicates a range of liability from \$120,101 to \$158,588 for liability insurance and \$122,112 to \$154,344 for worker's compensation. There has been no provision recorded for this assessment in the current year financial statements.

The District is exposed to various forms of loss of assets associated with the risks of fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, etc. Each of these risk areas are covered through the purchase of commercial insurance. The District has purchased certain policies, which are retrospectively rated, which includes workers' compensation insurance.

Under COBRA, employers are mandated to notify terminated employees of available continuing insurance coverage. Failure to comply with this requirement may put the school district at risk for a substantial loss (contingency). There were no instances of noncompliance noted.

NOTE 8 – RETIREMENT PLANS

Pension Plan

The Middlesboro Independent School System contributes to the Kentucky Teachers' Retirement System ("KTRS"), a cost-sharing, multiple employer defined benefit pension plan. KTRS administers retirement and disability annuities, and death and survivor benefits to employees and beneficiaries of employees of the public school systems and other public educational agencies in Kentucky. KTRS requires that members of KTRS occupy a position requiring either a four (4) year college degree or certification by KY Department of Education (KDE).

KTRS was created by the 1938 General Assembly and is governed by Chapter 181 Section 220 through Chapter 181 Section 990 of the Kentucky Revised Statutes (KRS). KTRS issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit pension plan. That report can be obtained by writing to the Kentucky Teachers' Retirement System, 479 Versailles Road, Frankfort, KY 40601 or from the KTRS web site at <http://ktrs.ky.gov/>.

Contribution rates are established by KRS. Members are required to contribute 10.855% of their salaries to KTRS. The Commonwealth of Kentucky is required to contribute 14.105% of salaries for members. The federal program for any salaries paid by that program pays the matching contributions. The Board is required to match 1.0% of salaries for all employees paid by the General fund.

The Middlesboro Independent School System's total payroll for the year was \$8,282,517. The payroll for employees covered under KTRS was \$6,381,161. For the year ended June 30, 2013, the Commonwealth contributed \$713,024 to KTRS for the benefit of participating employees. The School Districts' contribution to KTRS for the year ending June 30, 2013 was \$193,075, which represents those employees covered by federal programs.

Substantially all other employees (classified personnel) are covered under the County Employees Retirement System ("CERS"), a cost sharing, multiple-employer, public employers retirement system. Funding for the Plan is provided through payroll withholdings of 6% for employees hired after September 1, 2008 and 5% for employees hired before this date and a Board contribution of 19.55% of the employee's total compensation subject to contribution. The contribution requirement for CERS for the year ended June 30, 2013 was \$391,385, which consisted of \$309,531 from the Board and \$81,854 from the employees.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 8 – RETIREMENT PLANS (CONTINUED)

The "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the pensions' funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among the plans and employers.

CERS does not make separate measurements of assets and pension benefit obligation for individual employers. As the District is only one of several employers participating in the Plan, it is not practicable to determine the District's portion of the unfunded past service cost of the vested benefits of the District's portion of the Plan assets.

Medical Insurance Plan

In addition to the pension benefits described above, Kentucky Revised Statute 181.875 requires KTRS to provide post-retirement healthcare benefits to eligible members and dependents. The KTRS Medical Insurance benefit is a cost-sharing multiple employer defined benefit plan. Changes made to the medical plan may be made by the KTRS Board of Trustees, the Kentucky Department of Employee Insurance and the General Assembly.

To be eligible for medical benefits, the member must have retired either for service or disability. The KTRS Medical Insurance Fund offers coverage to members under the age of 65 through the Kentucky Employees Health Plan administered by the Kentucky Department of Employee Insurance. Once retired members and eligible spouses attain age 65 and are Medicare eligible, coverage is obtained through the KTRS Medicare Eligible Health Plan.

The post-retirement healthcare provided by KTRS is financed on a pay-as-you-go basis. In order to fund the post-retirement healthcare benefit, one and five tenths percent (1.5%) of the gross annual payroll of all active members is contributed. One-half (1/2) of this amount is derived from member contributions and one-half (1/2) from state appropriation. Also, the premiums collected from retirees, as described in the plan description, and investment interest help meet the medical expenses of the plan.

NOTE 9 – CONTINGENCIES

The District receives funding from federal, state and local government agencies and private contributions. These funds are to be used for designated purposes only. For government agency grants, if the grantor's review indicates that the funds have not been used for the intended purpose, the grantors may request a refund of monies advanced or refuse to reimburse the District for its disbursements. The amount of such future refunds and unreimbursed disbursements, if any, is not expected to be significant. Continuation of the District's grant programs is predicated upon the grantors' satisfaction that the funds provided are being spent as intended and the grantors' intent to continue their programs.

SHERRY STANDIFER, ET AL. VS. MIDDLESBORO INDEPENDENT SCHOOLS

Sherry Standifer, Statutory guardian and next friend of Kristen Standifer filed suit against the Middlesboro Public Schools, Superintendent Rita Cook, and Board Members Bill Johnson, Kelly Shoffner, Vickie Byrne, Kenny Pratt, and Edith Kelly on October 30, 2012. In the Complaint, the Plaintiff alleges that Kristen Standifer suffered pain of body and anguish of mind, permanent injury to an extent that she will suffer lost wages in the future as a result of a wall that was unsteady and fell, striking the Plaintiff on the head and neck. Interrogatories and Requests for Production of Documents have been propounded and answered. The deposition of Kristen Standifer was set for October 2, 2013, and mediation for this case was scheduled for September 25, 2013. There is insurance coverage for this claim through KSBIT. There was no provision for this contingency provided in the accompanying financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 10 – TRANSFER OF FUNDS

The following transfers were made during the year:

<u>Type</u>	<u>From Fund</u>	<u>To Fund</u>	<u>Purpose</u>	<u>Amount</u>
Operating	310	Debt Service	Debt service requirement	\$ 118,031
Operating	1	Special Revenue	Matching, Phase II	29,258
Operating	320	Debt Service	Debt service requirement	436,477
Operating	51	General	Indirect costs	37,488
Operating	320	Construction	Door hardware/ADA ramps	71,227

NOTE 11 – INTERFUND RECEIVABLES AND PAYABLES

There were no interfund receivables or payables at June 30, 2013.

NOTE 12 – DEFICIT OPERATING/FUND BALANCES

The District had a current year operating deficit in governmental funds, as follows:

Building/FSPK fund	<u>\$ (71,227)</u>
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NOTE 13 – SUBSEQUENT EVENTS

We evaluated events and transactions that occurred after the balance sheet date as potential subsequent events. We performed this evaluation through October 7, 2013, the date on which we issued our financial statements.

On August 30, 2013, the Middlesboro Board of Education unanimously voted to increase property taxes by 2.3 cents in an attempt to revive their school budget. According to board members, the tax increase comes as a way to help an ever dwindling school budget recoup what has been lost in coal severance money – money that the schools have relied on for many years. According to the Board, the increase could bring an extra \$100,000 to the District's budget – money that is needed to make ends meet without the severance money. The board also made sure the public was aware that compared to surrounding counties, the District is in the bottom when it comes to taxes and will remain there even with the tax increase. It was also pointed out that there has only been one other small tax increase in recent years – another aspect of taxes that sets the District apart from other school districts. Board members also shared various other ways they are trying to cut costs to improve the overall budget. Among ways the board is cutting costs is merging schools, energy auditing and salary limitations. Although the board says all of their efforts are helping, the tax increase is still necessary at this time.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
June 30, 2013

	Seek Capital Outlay <u>Fund</u>	FSPK <u>Fund</u>	Construction <u>Fund</u>	Debt Service <u>Funds</u>	Total Nonmajor Governmental <u>Funds</u>
ASSETS AND RESOURCES					
Cash and cash equivalents	\$ -	\$ 93,475	\$ 10	\$ -	\$ 93,485
TOTAL ASSETS AND RESOURCES	<u>\$ -</u>	<u>\$ 93,475</u>	<u>\$ 10</u>	<u>\$ -</u>	<u>\$ 93,485</u>
LIABILITIES AND FUND BALANCES					
Restricted					
Future construction projects	\$ -	\$ -	\$ 10	\$ -	\$ 10
Debt service	-	93,475	-	-	93,475
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ -</u>	<u>\$ 93,475</u>	<u>\$ 10</u>	<u>\$ -</u>	<u>\$ 93,485</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
Year Ended June 30, 2013

	Seek Capital Outlay Fund	FSPK Fund	Construction Fund	Debt Service Funds	Total Nonmajor Governmental Funds
REVENUES					
From local sources:					
Taxes					
Property	\$ -	\$ 222,894	\$ -	\$ -	\$ 222,894
Intergovernmental – state	<u>120,408</u>	<u>213,583</u>	<u>-</u>	<u>97,043</u>	<u>431,034</u>
TOTAL REVENUES	<u>120,408</u>	<u>436,477</u>	<u>-</u>	<u>97,043</u>	<u>653,928</u>
EXPENDITURES					
Payment of bonds	-	-	-	530,000	530,000
Payment of interest	-	-	-	121,551	121,551
Support services:					
District administration	<u>2,377</u>	<u>-</u>	<u>71,227</u>	<u>-</u>	<u>73,604</u>
TOTAL EXPENDITURES	<u>2,377</u>	<u>-</u>	<u>71,227</u>	<u>651,551</u>	<u>725,155</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>118,031</u>	<u>436,477</u>	<u>(71,227)</u>	<u>(554,508)</u>	<u>(71,227)</u>
OTHER FINANCING SOURCES (USES)					
Operating transfers in	-	-	71,227	554,508	625,735
Operating transfers out	<u>(118,031)</u>	<u>(507,704)</u>	<u>-</u>	<u>-</u>	<u>(625,735)</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>(118,031)</u>	<u>(507,704)</u>	<u>71,227</u>	<u>554,508</u>	<u>-</u>
NET CHANGES IN FUND BALANCES	-	(71,227)	-	-	(71,227)
FUND BALANCES, JULY 1, 2012	<u>-</u>	<u>164,702</u>	<u>10</u>	<u>-</u>	<u>164,712</u>
FUND BALANCES, JUNE 30, 2013	<u>\$ -</u>	<u>\$ 93,475</u>	<u>\$ 10</u>	<u>\$ -</u>	<u>\$ 93,485</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF RECEIPTS, DISBURSEMENTS AND FUND BALANCES – ACTIVITY FUNDS
MIDDLESBORO HIGH SCHOOL
Year Ended June 30, 2013

ACCOUNTS:	Cash Balances <u>July 1, 2012</u>	<u>Receipts</u>	<u>Disbursements</u>	<u>Interfund Transfers</u>
Activity Allotment	\$ 2,456	\$ -	\$ 1,547	\$ -
Athletics	27,076	77,156	83,512	-
Attendance	2	40	40	-
Audio Visual Club	100	-	-	-
Band	4	-	-	-
Beta Club	561	546	466	-
Choir	223	-	112	-
Class of 2013	1,285	61,145	61,364	575
DECA	3	-	-	-
Drama	58	-	-	-
FBLA	116	510	568	-
FCCLA (FHA)	75	-	67	-
FEA	198	-	-	-
General	9,766	34,267	33,068	(200)
Jacket Patch	133	-	104	-
JROTC	688	3,390	3,787	-
Journalism	719	17,125	16,704	150
Library	143	99	162	-
NFL	5	-	-	-
Parking	35	658	125	-
Prom	2,243	10,287	10,420	(725)
Student Council	916	-	290	-
Teachers	257	2,799	2,661	200
Technology	752	-	-	-
Textbooks	111	1,033	349	-
VICA	19	-	-	-
Year Book	5	-	-	-
Totals	<u>\$ 47,949</u>	<u>\$ 209,055</u>	<u>\$ 215,346</u>	<u>\$ -</u>

Cash Balances June 30, 2013	Accounts Receivable June 30, 2013	Accounts Payable June 30, 2013	Fund Balances June 30, 2013
\$ 909	\$ -	\$ -	\$ 909
20,720	-	-	20,720
2	-	-	2
100	-	-	100
4	-	-	4
641	-	-	641
111	-	-	111
1,641	-	-	1,641
3	-	-	3
58	-	-	58
58	-	-	58
8	-	-	8
198	-	-	198
10,765	291	-	11,056
29	-	-	29
291	-	-	291
1,290	-	-	1,290
80	-	-	80
5	-	-	5
568	-	-	568
1,385	-	-	1,385
626	-	-	626
595	53	111	537
752	-	-	752
795	-	-	795
19	-	-	19
5	-	-	5
<u>\$ 41,658</u>	<u>\$ 344</u>	<u>\$ 111</u>	<u>\$ 41,891</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF RECEIPTS, DISBURSEMENTS AND FUND BALANCES - ACTIVITY FUNDS
Year Ended June 30, 2013

	<u>Cash Balances</u> <u>July 1, 2012</u>	<u>Receipts</u>	<u>Disbursements</u>	<u>Interfund</u> <u>Transfers</u>
MIDDLESBORO MIDDLE SCHOOL				
All funds	<u>\$ 10,843</u>	<u>\$ 27,097</u>	<u>\$ 28,177</u>	<u>\$ -</u>
MIDDLESBORO PRIMARY SCHOOL				
All funds	<u>\$ 24,280</u>	<u>\$ 12,743</u>	<u>\$ 12,151</u>	<u>\$ -</u>
MIDDLESBORO INTERMEDIATE SCHOOL				
All funds	<u>\$ 33,301</u>	<u>\$ 11,490</u>	<u>\$ 21,785</u>	<u>\$ -</u>

Cash Balances June 30, 2013	Accounts Receivable June 30, 2013	Accounts Payable June 30, 2013	Fund Balances June 30, 2013
<u>\$ 9,763</u>	<u>\$ 10</u>	<u>\$ 1,128</u>	<u>\$ 8,645</u>
<u>\$ 24,872</u>	<u>\$ 67</u>	<u>\$ 139</u>	<u>\$ 24,800</u>
<u>\$ 23,006</u>	<u>\$ 1,574</u>	<u>\$ -</u>	<u>\$ 24,580</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2013

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Program or Award</u>	<u>Federal Disbursements</u>
<u>U.S. Department of Education</u>				
Passed through State Department of Education:				
SPECIAL EDUCATION CLUSTER (IDEA)				
Special Education – Grants to States (IDEA, Part B)	84.027A	3810002-12	\$ 328,493	\$ 315,979*
Special Education – Grants to States (IDEA, Part B)	84.027	3810002-11	344,511	26,168*
Special Education – Preschool Grants (IDEA, Preschool)	84.173	3800002-12	20,115	18,350*
Special Education – Preschool Grants (IDEA, Preschool)	84.173	3800002-11	20,215	428*
Total Special Education Cluster (IDEA)				<u>360,925</u>
TITLE I, PART A CLUSTER				
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100002-12	952,335	842,280*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100002-11	961,771	105,967*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010A	3100202-11	49,737	28,974*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100102-12	8,243	5,295*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100202-10	71,643	402*
Total Title I, Part A Cluster				<u>982,918</u>
EDUCATIONAL TECHNOLOGY STATE GRANTS CLUSTER				
Education Technology State Grants	84.318	3210002-10	2,942	29
Total Educational Technology State Grants Cluster				<u>29</u>
SCHOOL IMPROVEMENT GRANTS CLUSTER				
School Improvement Grants	84.377	3100302-09	250,000	100,802
Total School Improvement Grants Cluster				<u>100,802</u>

* Denotes major program

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)
Year Ended June 30, 2013

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Program or Award</u>	<u>Federal Disbursements</u>
<u>U.S. Department of Education</u>				
Vocational Education – Basic Grants to States	84.048	4621332-13	24,733	14,984
Vocational Education – Basic Grants to States	84.048	4621232-11	20,401	8,380
Vocational Education – Basic Grants to States	84.048	4621132-10	19,659	450
Improving Teacher Quality State Grants	84.367A	3230002-12	124,141	114,279
Improving Teacher Quality State Grants	84.367A	3230002-11	125,425	7,245
Improving Teacher Quality State Grants	84.367	3230002-10	145,547	4,364
Twenty-First Century Community Learning Centers	84.287	3400002-11	60,000	57,629
Twenty-First Century Community Learning Centers	84.287	3400002-10	5,000	759
Twenty-First Century Community Learning Centers	84.287	3400002-10	84,300	10,678
Rural Education	84.358	3140002-12	25,753	5,000
Rural Education	84.358	3140002-11	31,306	16,042
Education Jobs Fund	84.410	EJ0800-10	387,277	11,367
Race To The Top	84.413A	4521	38,784	<u>25,809</u>
Total U.S. Department of Education				<u>\$ 1,721,660</u>
<u>U.S. Department of Agriculture</u>				
Passed through State Department of Education:				
CHILD NUTRITION CLUSTER				
National School Breakfast Program	10.553	7760005-13	\$ 197,263	\$ 197,263*
	10.553	7760005-12	54,319	54,319*
National School Lunch Program	10.555	7750002-13	406,805	406,805*
	10.555	7750002-12	107,842	107,842*
Summer Food Service Program for Children	10.559	7740023-13	22,695	22,695*
Summer Food Service Program for Children	10.559	7740023-12	16,935	16,935*
Summer Food Service Program for Children	10.559	7690024-12	1,751	<u>1,751*</u>
Total Child Nutrition Cluster				<u>807,610</u>
EMERGENCY FOOD ASSISTANCE CLUSTER				
Emergency Food Assistance Program	10.569	4002827	46,719	<u>46,719</u>
Total Emergency Food Assistance Cluster				<u>46,719</u>
Fresh Fruit and Vegetable Program	10.582	7720012-13	29,184	29,184
	10.582	7720012-12	8,189	<u>8,189</u>
Total U.S. Department of Agriculture				<u>\$ 891,702</u>

* Denotes major program

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)
Year Ended June 30, 2013

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Program or Award</u>	<u>Federal Disbursements</u>
<u>U.S. Department of Defense</u>				
Junior Reserve Officers' Training Corps	12.000	5043	\$ 66,856	<u>\$ 66,856</u>
Total U.S. Department of Defense				<u>\$ 66,856</u>
<u>Appalachian Regional Commission</u>				
Appalachian Research, Technical Assistance and Demonstration Project	23.011	6883	\$ 4,125	\$ 3,040
Appalachian Research Technical Assistance and Demonstration Project	23.011	6882	5,000	<u>875</u>
Total Appalachian Regional Commission				<u>\$ 3,915</u>
Total Expenditures of Federal Awards				<u>\$ 2,684,133</u>

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Middlesboro Independent School District and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
June 30, 2013

SUMMARY OF AUDIT RESULTS

1. We have issued an unmodified opinion on the basic financial statements of the Middlesboro Independent School District.
2. No material weakness(es) were identified in our audit of the financial statements.
3. No significant deficiencies were identified in our audit of the financial statements.
4. No material noncompliance was identified in our audit of the financial statements.
5. No material weakness(es) were identified in our audit of internal control over major programs.
6. No significant deficiencies were noted in our audit of internal control over major programs.
7. We have issued an unmodified opinion on compliance for major programs.
8. The audit did not disclose any audit findings, which we are required to report under Section 510(a) of OMB Circular A-133.
9. The programs tested as major programs included:

	<u>CFDA</u>
TITLE I, PART A CLUSTER	
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010A
CHILD NUTRITION CLUSTER	
National School Lunch Program	10.555
Summer Food Service Program for Children	10.559
National School Breakfast Program	10.553
SPECIAL EDUCATION CLUSTER (IDEA)	
Special Education – Preschool Grants (IDEA, Preschool)	84.173
Special Education – Grants to States (IDEA, Part B)	84.027
Special Education – Grants to States (IDEA, Part B)	84.027A

10. The threshold for distinguishing Types A and B programs was \$300,000.
11. Middlesboro Independent School District was determined to be a low risk auditee.

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

None

FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

None

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
June 30, 2013

NONE

Marr, Miller & Myers, PSC

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

October 7, 2013

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

We have audited, in accordance with U.S. generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; the provisions of Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations; Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the Independent Auditor's Contract – State Audit Requirements, Appendix III to the Independent Auditor's Contract – Audit Extension Request and Appendix IV to the Independent Auditor's Contract – Instructions for Submission of the Audit Report, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Middlesboro Independent School District, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated October 7, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Marr, Miller & Myers, PSC

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. In addition, the results of our tests disclosed no instances of material noncompliance of specific state statutes or regulations identified in Appendix II of the Independent Auditor's Contract – State Audit Requirements.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Marr, Miller & Myers, PSC

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

October 7, 2013

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

Report on Compliance for Each Major Federal Program

We have audited Middlesboro Independent School District's compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2013. The District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the District's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with U.S. generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; the provisions of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations; Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the Independent Auditor's Contract – State Audit Requirements, Appendix III to the Independent Auditor's Contract – Audit Extension Request and Appendix IV to the Independent Auditor's Contract – Instructions for Submission of the Audit Report. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the District's compliance.

Marr, Miller & Myers, PSC

Opinion on Each Major Federal Program

In our opinion, the District, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2013.

Report on Internal Control Over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Marr, Miller & Myers, PSC

Certified Public Accountants

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P.O. Box 663
Corbin, Kentucky 40702

October 7, 2013

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

In planning and performing our audit of the financial statements of the Middlesboro Independent School District for the year ended June 30, 2013, we considered the District's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure. We noted no items that need to be communicated to management.

Marr, Miller & Myers, PSC

Certified Public Accountants